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TO RUEHC/SECSTATE WASHDC 4794
RHEHAAA/NATIONAL SECURITY COUNCIL WASHINGTON DC
RUEHZU/APEC COLLECTIVE
RUEHBY/AMEMBASSY CANBERRA 3486
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RUEHRH/AMEMBASSY RIYADH 0007
RUEHDN/AMCONSUL SYDNEY 2024
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UNCLAS SECTION 01 OF 03 MELBOURNE 000125

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E.O. 12958: N/A

TAGS: [EIND](#) [ECON](#) [ETRD](#) [AS](#)

SUBJECT: Australian Auto Industry Braces for Tough Times

REF: Canberra 100; Canberra 1079

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Summary

1. (SBU) The Australian automotive industry, headquartered in Victoria, is in for tough times. With Toyota worried, GM/Holden pressed and Ford on the ropes, industry leaders are expressing concern over the future of Australia's biggest manufacturing industry. A perfect storm is brewing for an auto industry facing tightening credit, changing consumer tastes, lower tariffs, a domestic components market on the rocks, trouble in the U.S. parent headquarters all compounded by what was already a cyclical downturn in the industry. Pessimistic predictions of the end of the Australian auto industry still appear to be premature, but there is anxiety in Port Melbourne. End Summary.

Trouble Ahead

2. (SBU) Contacts at GM/Holden, Toyota and the Victorian Government told ConGen pol/econoff and visiting Embassy Canberra econ officer on October 29 that the Australian automotive industry is in for tough times. According to GM/Holden's Associate Director for Government Affairs, Samantha Read, the automobile market in Australia is "softening" in part due to the international financial crisis and concern over what it will mean for Australia. She said GM/Holden, which celebrates its 60th anniversary in November, has seen a 10 percent drop in sales over the last quarter and anticipates that third quarter figures will be worse yet.

3. (SBU) Toyota's Manager for Government Affairs, Peter Griffin was more upbeat in expectations for his company. Griffin anticipates that the global financial crisis may result in reduced consumer spending over the next few years, but said that he is uncertain how this will affect the Australian auto industry. He believes that the total Australian market for cars (sales exceeded one million in 2007 for the first time) will contract in 2008-09. The very strong (until recently) Australian dollar hurt Toyota (and Holden) exports, so the recent drop in the Australian dollar (ref B) was welcome; Griffin said the "sweet spot" for the Australian dollar from Toyota's perspective was around US80 cents. Griffin was concerned about Ford and GM/Holden; Toyota needs other auto manufacturers to maintain a sufficiently large platform for the auto industry. "Having four companies was really good," Griffin said, alluding to the now-expired Mitsubishi Australia, "we don't want to have fewer than three."

4. (SBU) Ray Doyle and Geoff Susans of the Industry and Trade Division in Victoria's Department of Innovation, Industry and

Regional Development (DIIRD) painted a far grimmer picture. Doyle said Ford, which announced that it will scale back production in Australia by 20 percent starting November 4, is in a "weak position" to come through the current downturn. Difficulties in obtaining financing for new car sales have clogged dealership floors and reduced franchise profits; Doyle said sales are so poor that there are ships with new cars waiting at the port because there is "no room" for additional cars in the receiving facilities. The automotive industry is anxiously awaiting the Commonwealth government's response to the report of the auto industry chaired by former Victoria Premier Steve Bracks (which could be out this week).

Analysts within the Industry and Trade Division, however, predict that any government assistance to Victoria's automotive industry may be "too little, too late."

Keeping Up With a Changing Market

15. (SBU) The six cylinder sedan - the iconic Holden Commodore and Ford Falcon - has traditionally been Australia's car of choice; GM/Holden and Ford are heavily invested in these models. But higher fuel costs and concern over greenhouse gas emissions are leading more Australians to prefer smaller and more fuel efficient vehicles, (these same factors made Mitsubishi's six-cylinder M380 model unprofitable from the beginning, reftel), while growing SUV sales have squeezed the six cylinder sedans at the top end of the market. Ford Australia and GM/Holden are poorly positioned to keep up with changing consumer demands. Neither manufactures a four cylinder model in Australia (the Toyota Camry is the only locally produced four cylinder car). While Ford Australia hopes to begin producing the four cylinder Focus model in Victoria in 2011, some observers worry that it might be too late. Toyota will begin producing a hybrid Camry in Australia in late 2009, taking advantage of a new GOA "green car" incentive program. Griffin told us that, contrary

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to media reports from earlier this year when the award was made, the A\$35 million grant was "decisive" in Toyota's decision to produce those hybrids in Australia.

Finance Drying Up

16. (SBU) Responding to the international financial crisis and credit crunch, both GMAC (General Motors Acceptance Corporation) and GE (General Electric) announced in October that they would cease to provide car financing services in Australia. According to GM/Holden, GMAC provided 45 percent of financing for new Holden purchases and their withdrawal is already having an impact. The limited financing available to dealerships and franchises has led to a sharp decline in new car sales. Dealers, according to Doyle at Victoria DIIRD, are considering auctioning some of their stock at below-market prices in order to move inventory and stay afloat; this sort of move would not help pull through additional vehicles from factories. In a private forum held on October 13, Steve Bracks noted that access to finance will be a "major challenge" for the auto industry due to the tightening of credit.

17. (SBU) Scarce credit is also impacting Australia's fragile components manufacturing sector. Criticized for being too fragmented and lacking the scale necessary to compete with foreign manufacturers, Australia's automotive component sector is in "real trouble" says the Australian Industry Group (AIG). According to Innes Willox, AIG's Director for International Relations, automotive components manufacturers cannot access capital to fund mergers and carry out business because banks consider these companies to be too "risky." One component manufacturer employing 300 people has already gone under and Willox fears that others may follow suit. (Note: The components sector is a key part of Australia's vertically integrated automotive industry. Many components for domestically produced vehicles are sourced locally from these companies. If they go under, there would be little economic reason to assemble autos in Australia from foreign-sourced components. End note.)

Importance of the Middle East

¶8. (SBU) Foreign markets are critical for Toyota, which exports 70 percent of its Australian production, and GM/Holden, which exports 50 percent (by contrast, Ford only exports 5000 cars a year, to New Zealand - leaving it nearly 100 percent reliant on the small Australian market). For both Toyota and GM/Holden, the Middle East is the primary export destination for domestically manufactured automobiles. This was a key reason Australia began negotiations with the Gulf Cooperation Council for an FTA. But, according to DIIDR's Doyle, Saudi Arabia has held up a potential FTA with Australia even though it has no domestic automobile manufacturing sector to protect because they are thinking of making cars in the future. Should a major car producer like Japan win a preferential trade deal with Saudi Arabia and the GCC, AIG's Willox said, Australia's share of that significant market would find itself in very rough waters.

Snapshot of the Australian Auto Industry

¶9. (SBU) Automobiles are Australia's largest manufactured export (US\$4 billion). The industry employs approximately 64,000 people. In 2007, Australian parts and accessory imports from the United States were valued at \$402 million, an increase of 12 percent from 2006, and total car sales were approximately 1,049,000. Currently, 81 percent of automobiles sold in Australia are imports; domestic industry produces approximately 300,000, many of which are exported. The collapse of Mitsubishi Australia in February 2008 (reftel) left Australia with three car companies: Ford, GM/Holden and Toyota.

¶10. (U) The automotive industry is of strategic importance to the Australian economy. Major macroeconomic factors such as growth, employment, technological progress and the rate of innovation are all strongly influenced by the automotive industry. It is a key driver of economic growth and provides large benefits to the economy through the education and training of employees; the introduction of new technologies; design and engineering capabilities; operational and managerial concepts; and its contribution to further global integration.

Comment

¶11. (SBU) Most observers expect that Australian tariffs on

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automobiles will be lowered in 2010 according to schedule from 10 percent to 5 percent. Industry leaders expect some measure of government assistance to accompany the reduction in tariffs, but some are expressing concern over a perfect storm in the auto industry. Tightening credit, changing consumer tastes, lower tariffs, a domestic components market on the rocks, and trouble in the U.S. parent headquarters are compounding what was already a cyclical downturn in Australia's automotive industry. While pessimistic predictions of the end of Australia's auto industry still appear premature, anxiety and uncertainty about the industry's future are pervasive.

THURSTON